

**VIRGINIA POLYTECHNIC INSTITUTE
AND STATE UNIVERSITY
BLACKSBURG, VIRGINIA**

**REPORT ON AUDIT
FOR THE YEAR ENDED
JUNE 30, 2001**



AUDIT SUMMARY

Our audit of Virginia Polytechnic Institute and State University for the year ended June 30, 2001, found:

- the financial statements are presented fairly, in all material respects;
- internal control matters that we consider to be reportable conditions; however we do not consider any of these to be material weaknesses;
- no instances of noncompliance required to be reported; and
- adequate corrective action of prior audit findings except for the prior year finding titled "Ensure Departments Follow Financial Policies and Procedures."

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October 12, 2001

The Honorable James S. Gilmore, III
Governor of Virginia

The Honorable Vincent F. Callahan, Jr.
Chairman, Joint Legislative Audit
and Review Commission

The Board of Visitors
Virginia Polytechnic Institute and
State University

INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE AND ON
INTERNAL CONTROL OVER FINANCIAL REPORTING

We have audited the financial statements of **Virginia Polytechnic Institute and State University** as of and for the year ended June 30, 2001, and have issued our report thereon dated October 12, 2001. Our report on the financial statements is contained in the President's Report 2000-2001 issued by the University. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States.

Management's Responsibility

The University's management has responsibility for establishing and maintaining internal control and complying with applicable laws and regulations. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of controls. Internal control is a process designed to provide management with reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition; transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of the financial statements in accordance with generally accepted accounting principles; and the University has complied with applicable laws and regulations.

Compliance

As part of obtaining reasonable assurance about whether the University's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination

of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under Government Auditing Standards. However, we noted certain immaterial instances of noncompliance that we have reported in the section entitled, "Internal Control and Compliance Findings and Recommendations."

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the University's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. However, we noted certain matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the University's ability to record, process, summarize and report financial data consistent with the assertions of management in the financial statements. Reportable conditions are described in the section entitled, "Internal Control and Compliance Findings and Recommendations."

We believe none of the reportable conditions described above are material weaknesses. A material weakness is a condition in which the design or operation of one of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses.

Status of Prior Findings

The University has taken adequate corrective action with respect to audit findings reported in the prior year except for the prior year finding entitled "Ensure Departments Follow Financial Policies and Procedures."

Exit Conference and Report Distribution

We discussed this report with management at an exit conference held on October 24, 2001. This report is intended solely for the information and use of the Governor and General Assembly, Board of Visitors, audit committee, and management, and is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited.

AUDITOR OF PUBLIC ACCOUNTS

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INTERNAL CONTROL AND COMPLIANCE FINDINGS AND RECOMMENDATIONS

Status of University Initiative to Ensure Departments Follow Financial Policies and Procedures

In our prior and several previous audits, we raised significant concerns that University departments frequently do not follow financial policies and procedures. A significant portion of our concerns resulted from academic departments failing to either understand or adhere to University policies and procedures. We recommended that University's executive management work together to develop a stronger training, monitoring, and enforcement program with appropriate consequences.

Under the leadership of the Executive Vice-President, the University established a response team that included members from the controller's office, budget and financial management, leadership development, personnel services, office for special initiatives and internal audit. The response team began meeting in May 2001 and has developed the framework of a comprehensive program with six broad initiatives to address our concerns. As the completion date for a large portion of the program is not until 2002, we again found similar noncompliance in our testwork in 28 departments this year. Listed below are the six initiatives and completion timelines where known.

1. Encourage compliance with University policies and procedures.

The response team has proposed to include administrative performance as an evaluation criterion for all administrators and faculty members, including academic department heads and directors. If adopted, department heads and other administrators will receive administrative performance criteria by January 2002 for inclusion in the Fall 2003 Faculty Merit Review Process.

2. Directly assist departments in achieving good business practices.

By January 2002, the University will publish a Departmental Business Management Guide and hire a business practices specialist to assist departments and monitor department compliance.

3. Develop incentive programs to encourage and reward good business practices.

By the end of the 2002-2003 academic year, the University will develop a series of incentive programs including an award for administrative excellence, a revised rewards and recognition policy with improved ability to reward exceptional administrative employees, and grants to departments for the development of programs, systems, or processes supporting good business practices and administrative excellence.

4. Develop management monitoring reports to identify areas of concern.

Reports will focus on inventory tracking, leave reporting, small purchase cards, late termination notices and split purchase orders. There is no estimated completion date, as several items require resolution.

5. Training and Professional Development

The University recently implemented two comprehensive certificate programs in fiscal and human resource practices for employees in administrative and business support staff and professional roles. In addition, the University is developing and implementing training programs that include enhancing and expanding current administrative and financial training, a new training program for research administrators, a training program for new researchers, a business practices seminar for

research center directors and their financial and business managers and the establishment of an Administrators Development Institute. The projected completion date for these programs is Summer 2002.

6. Improve communications with departmental administrators and fiscal staff.

The Vice President for Budget and Financial Management will direct the implementation of a communications program to improve two-way information flow between deans, directors, and department heads and their fiscal officers. The communications will include periodic meetings between the Vice President and fiscal officers to re-emphasize compliance with University policies and procedures. These meetings will also allow the Vice President to gain a better understanding of the issues facing fiscal officers.

The University should commit adequate resources to complete the program implementation according to established timelines. Executive management should review and formally approve the response team's initiatives and monitor their completion. We believe the University's success depends on implementing a program that sufficiently addresses and balances training, incentives, monitoring, and enforcement. We concur with the implementation team's initiatives and their proposal to include administrative performance as an employee evaluation criterion. The implementation team under the direction of executive management should continue to develop the foundation of an enforcement program that includes appropriate consequences for noncompliance. If training and incentives fail to ensure compliance, it is critical that the University implement a strong enforcement program with appropriate consequences to address repeated problems identified in its monitoring program.

Properly Calculate Allocation of Title IV Refunds

The University's Student Information System does not properly calculate Title IV refund allocations for students with adjustments to their original institutional charges. In Fall 2000, the University implemented the new federally mandated refund policy for students receiving Title IV funds who withdraw from classes. This new policy sets forth a formula to determine the responsibility for the refund between the University and the student. The System calculates refund allocations using original institutional charges rather than adjusted charges. Using original charges results in an improper allocation of responsibility between the University and the student.

The University should recalculate refund allocations for all students with adjustments to institutional charges since Fall 2000 and make appropriate settlements. The University should work with its Student Information System vendor to determine the cause of this improper allocation and request or make changes to the software to prevent miscalculations in the future.

Review and Strengthen Procedures for Federal Perkins Loan Program Drawdowns

The University Bursar did not comply with federal regulations and established procedures for drawdown of the federal Perkins capital contribution. Failure to follow federal regulations for drawdowns could lead to financial penalties or the Department of Education placing the University on a more restrictive drawdown method such as cash reimbursement. Details of the noncompliance follow:

- The Bursar held \$214,577 in excess federal funds from August 16, 2000 until June 15, 2001, when the Bursar returned the funds to the Department of Education. The Bursar failed to follow established cash forecasting procedures for determining immediate cash needs for drawdowns. Although the University held \$1,322,822 in Perkins collections and projected disbursements of

only \$611,000, the Bursar requested the entire federal contribution allocation for the year on August 15. Federal regulations require institutions to limit drawdowns of federal funds to immediate cash needs and to use the funds within a three day time period.

- The Bursar did not record the August 15 drawdown in the accounting system until September 29 and did not transfer the funds from the consolidated local funds bank account to the Perkins bank account until October 20. Federal regulations require institutions to deposit the capital contribution into a separate interest bearing Perkins fund.
- The Bursar did not deposit the institutional matching funds for the August 15 drawdown until October 3, 2000. Federal regulations require that institutions deposit their matching capital contribution before or at the same time they deposit their federal capital contribution.

The Bursar should re-examine procedures for Perkins drawdowns and determine why her office failed to comply with established procedures and federal regulations. The Bursar should ensure that employees understand Perkins drawdown procedures and how to obtain the needed information from the new receivables and financial aid systems to ensure compliance in the future.

Review Administration of Perkins Loan Program

The Office of Scholarships and Financial Aid did not award \$235,776 in authorized Perkins funds. The failure to award the entire Perkins allocation not only impacts assistance to students during the year, but also may reduce the federal contribution in future years. The University requested a waiver for the loss of future federal contribution.

The Financial Aid Director and the Bursar have recently begun reviewing procedures and timelines to incorporate a better coordination of efforts between their offices to provide improved awarding and management of these funds. The Financial Aid Director and Bursar should complete their review of the Perkins procedures and timelines and carefully monitor the administration of the program to ensure that their corrective action achieves the desired results.

Charge Interest on Delinquent Receivables

The Bursar does not charge interest and late fees on delinquent receivables as recommended by Section 20.505 of the Commonwealth Accounting Policies and Procedures Manual. The new receivables system could not automatically compute these charges and the Bursar determined it was impractical to compute these charges manually. The University should commit the resources and priority necessary to enhance the new receivables system to compute interest and late fees on delinquent accounts to encourage prompt payment.

VIRGINIA POLYTECHNIC INSTITUTE AND STATE UNIVERSITY

Blacksburg, Virginia

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